

Research Update:

# Regional Municipality Of York 'AA+' Ratings Affirmed; Outlook Positive

July 27, 2020

## Overview

- We believe the Regional Municipality of York's diverse economy and relatively wealthy residents will support regional revenues and help insulate the region from the economic impacts of the COVID-19 pandemic.
- We expect York's operating surplus will temporarily decline in 2020, and that transfers to the region's reserves might also fall.
- Furthermore, we expect that York will be able to maintain its capital spending program and continue to limit its debt issuance to levels below the peak in 2017.
- Accordingly, we are affirming our 'AA+' long-term issuer credit and senior unsecured debt ratings on York and maintaining the positive outlook.

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## Rating Action

On July 27, 2020, S&P Global Ratings affirmed its 'AA+' long-term issuer credit and senior unsecured debt ratings on the Regional Municipality of York and maintained the positive outlook.

## Outlook

The positive outlook reflects the possibility that, despite the pandemic, we could raise the rating to 'AAA' should economic growth continue to support a larger assessment base and that a high level of growth-related capital revenue supports York's evolving capital program. Under these circumstances, York could maintain its strong after-capital surpluses and reduce the need for external financing such that its tax-supported debt burden stays below 120% of consolidated operating revenues through 2021, and sustaining an interest burden of less than 5%. We would also expect the region to carefully monitor its finances, growth, and development charge collections to ensure capital spending remains consistent with population growth, and to amend its capital plan if necessary, before we would consider raising the rating in the next year.

We could revise the outlook to stable if, in the next year, management's commitment to fiscal

sustainability weakened in the face of slower economic growth or a desire for elevated capital spending, resulting in weaker-than-expected operating balances, sustained after-capital deficits, or a rising debt burden that kept interest expenses above 5% of revenues.

## **Rationale**

We expect the COVID-19 pandemic-related restrictions and economic impact will have limited implications for York's finances. The region benefits from a strong and stable property tax base as its primary source of revenue. We expect the region could have lower fee and other non-tax revenues as well as higher expenses, including public health spending, which will likely lead to lower operating and after-capital surpluses. We expect the region will maintain its plan to limit debt issuances to levels below the peak in 2017.

The ratings also reflect the region's strong financial management, which we believe will guide York through difficult economic times prudently and maintain the region's financial sustainability. The ratings also reflect the region's strong and diverse economy, which should continue to support regional revenues. York's slowing accumulation of debt and exceptional liquidity also support the ratings.

## **A diverse economy supports York's revenues; very strong management and institutional framework also boost the ratings.**

Our very strong economic assessment reflects our belief that, despite the pandemic and related economic impact, York's diverse and wealthy economy will continue to support GDP per capita above the national average and growth in line with that of Canada. York's economy benefits from its proximity to and integration with the City of Toronto. The region boasts the sixth-largest municipal population in Canada, with an estimated 1.2 million residents in 2019, as well as a sizable employment base of 654,650 jobs. Recent population growth has been manageable, in the 1%-2% range per year. Building activity and assessment growth have been robust and will continue to support revenue growth. Furthermore, York's well-diversified economy should continue to support revenue growth throughout the business cycle, in our view. Assessment growth has averaged about 2% over the past five years.

We believe York's financial management is very strong and in line with that of regional peers. York's long-term capital plan has evolved in the past several years, reflecting both revised growth estimates and greater financial discipline, and we believe management demonstrates the flexibility to appropriately align capital plans with fluctuations in population growth. The region produces a multiyear budget that matches the term of council and from which management develops annual budgets with achievable revenue and expenditure targets. Moreover, the region has an established commitment to fiscal sustainability through its fiscal strategy process, which successive regional councils have endorsed.

As do other Canadian municipalities, York operates under a very predictable and well-balanced institutional framework. The provincial government imposes fiscal restraint through legislative requirements to pass balanced operating budgets. At the same time, provincial-municipal relationships have been more dynamic than the federal-provincial one, largely because municipal governments are established through provincial statute and not the constitution. In that regard, we expect York's relationship with Ontario will continue to be supportive.

**Strong revenue generation and related budgetary surpluses support creditworthiness, while we expect the debt burden will remain stable in the next two years.**

York typically generates large operating surpluses, propelled by its rising population and assessment values. We expect the region to continue generating strong and stable operating balances at about 24% of operating revenues in our base-case scenario for 2018-2022. Furthermore, these surpluses should support York's capital plans and result in after-capital surpluses of about 8.7% of total revenues. The region has allocated some of its surpluses to capital reserves to minimize related debt issuance. We view York as having high budgetary flexibility, owing to its above-average household incomes and relatively low tax rates, which we think would support additional regional revenue generation, if necessary.

We expect annual surpluses and strong reserves will help fund the region's capital plan and reduce York's reliance on debt funding. We expect capital spending will average about \$600 million per year through 2022, with spending focused on roads, transit, and, to a lesser degree, water and wastewater. The current 10-year capital plan allocates C\$7.1 billion to capital projects, of which 35% will be debt-financed. Management expects reserves to contribute the bulk of capital funding. We expect York's debt burden (net of sinking funds) will remain stable at 106.7% of consolidated operating revenue in 2022. Interest averages 4.8% of operating revenues.

York demonstrates exceptional liquidity, with liquidity balances that significantly exceed debt servicing requirements. We believe that cash and investment balances (excluding long-term net sinking funds and deferred revenue) will total almost C\$3.1 billion in the next 12 months, sufficient to cover over 1,020% of the total debt service forecast. We believe York's access to external liquidity is strong, in part because of its frequent issuance and its practice of maintaining benchmark issues that bolster liquidity for its debt in the secondary markets. Although the region's capital expenditure plans could cause near-term liquidity to fluctuate, we expect ongoing efforts to build capital reserves will support the liquidity position in the next two years.

**Key Statistics**

Table 1

**Regional Municipality of York -- Selected Indicators**

(Mil. C\$)	--Year ended Dec. 31--					
	2017	2018	2019	2020bc	2021bc	2022bc
Operating revenues	2,240	2,381	2,537	2,495	2,660	2,779
Operating expenditures	1,707	1,892	1,837	1,954	1,985	2,073
Operating balance	533	489	700	541	675	706
Operating balance (% of operating revenues)	23.8	20.5	27.6	21.7	25.4	25.4
Capital revenues	207	306	170	180	90	128
Capital expenditures	643	344	637	633	583	590
Balance after capital accounts	96	451	233	88	181	245
Balance after capital accounts (% of total revenues)	3.9	16.8	8.6	3.3	6.6	8.4

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Table 1

### Regional Municipality of York -- Selected Indicators (cont.)

(Mil. C\$)	--Year ended Dec. 31--					
	2017	2018	2019	2020bc	2021bc	2022bc
Debt repaid	191	161	174	177	189	206
Gross borrowings	300	40	349	162	252	341
Balance after borrowings	206	329	408	73	245	380
Direct debt (outstanding at year-end)	3,044	2,898	2,833	2,795	2,844	2,948
Direct debt (% of operating revenues)	135.9	121.7	111.7	112.0	106.9	106.1
Tax-supported debt (outstanding at year-end)	3,044	2,898	2,833	2,795	2,844	2,948
Tax-supported debt (% of consolidated operating revenues)	135.9	121.7	111.7	112.0	106.9	106.1
Interest (% of operating revenues)	6.1	5.6	5.0	4.8	4.5	4.5
National GDP per capita (single units)	58,591	60,011	61,291	57,181	60,677	63,026

The data and ratios above result in part from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information. The main sources are the financial statements and budgets, as provided by the issuer. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario. N/A--Not applicable.

## Ratings Score Snapshot

Table 2

### Regional Municipality of York -- Ratings Score Snapshot

Key rating factors	Scores
Institutional framework	2
Economy	1
Financial management	1
Budgetary performance	1
Liquidity	1
Debt burden	3
Stand-alone credit profile	aa+
Issuer credit rating	AA+

S&P Global Ratings bases its ratings on non-U.S. local and regional governments (LRGs) on the six main rating factors in this table. In the "Methodology For Rating Local And Regional Governments Outside Of The U.S.," published on July 15, 2019, we explain the steps we follow to derive the global scale foreign currency rating on each LRG. The institutional framework is assessed on a six-point scale: 1 is the strongest and 6 the weakest score. Our assessments of economy, financial management, budgetary performance, liquidity, and debt burden are on a five-point scale, with 1 being the strongest score and 5 the weakest.

## Key Sovereign Statistics

- Sovereign Risk Indicators, July 14, 2020. An interactive version is available at <http://www.spratings.com/sri>

## **Related Criteria**

- Criteria | Governments | International Public Finance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

## **Related Research**

- Public Finance System: Canadian Municipalities, May 12, 2020
- COVID-19 Causes More Severe Disruption For Canada's Economy, April 17, 2020
- Guidance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- Institutional Framework Assessments For International Local And Regional Governments, July 4, 2019
- Canada's Economy Faces A Patchy Recovery, June 29, 2020

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee's assessment of the key rating factors is reflected in the Ratings Score Snapshot above.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria And Research').

## **Ratings List**

### **Ratings Affirmed**

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#### **York (Regional Municipality of)**

Issuer Credit Rating AA+/Positive/--

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#### **York (Regional Municipality of)**

Senior Unsecured AA+

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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at [www.standardandpoors.com](http://www.standardandpoors.com) for further information. Complete ratings information is available to subscribers of RatingsDirect at [www.capitaliq.com](http://www.capitaliq.com). All ratings affected by this rating action can be found on S&P Global Ratings' public website at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search box located in the left column.

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